

**Audit Reconsideration Cases Create
Unnecessary Burden on Taxpayers and the
Internal Revenue Service**

March 2001

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This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

March 9, 2001

MEMORANDUM FOR COMMISSIONER ROSSOTTI

A handwritten signature in cursive script that reads "Pamela J. Gardiner".

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Audit Reconsideration Cases Create
Unnecessary Burden on Taxpayers and the Internal Revenue
Service

This report presents the results of our review of the Internal Revenue Service's (IRS) system of controls over the audit reconsideration process. In summary, we found that audit reconsideration cases create an unnecessary burden on both the taxpayer and the IRS. The IRS does not currently have an adequate system in place to measure the total volume of audit reconsideration cases. As a result, it cannot systemically determine the specific causes of these cases in order to develop and implement corrective actions to reduce the number of future audit reconsiderations.

We recommended that the IRS improve its proposed management information reports to accurately account for the total volume of audit reconsideration cases and to identify their related account characteristics to determine their cause. Management agreed to the recommendation we presented. Management's comments have been incorporated into the report where appropriate, and the full text of their comments is included as an appendix.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions, or your staff may call Walter Arrison, Associate Inspector General for Audit (Wage and Investment Income Programs), at (770) 936-4590.

**Audit Reconsideration Cases Create Unnecessary Burden
on Taxpayers and the Internal Revenue Service**

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Audit Reconsideration Cases Create Unnecessary Burden on Taxpayers and the Internal Revenue Service

Executive Summary

Audit reconsideration cases¹ create an unnecessary burden on both the taxpayer and the Internal Revenue Service (IRS). In Fiscal Year (FY) 1999 alone, the IRS abated audit assessments on the accounts of approximately 106,000 individual taxpayers through its audit reconsideration process. This represents a burden on taxpayers because it requires them to address excessive tax assessments that should have been resolved during the initial audit. The IRS is also burdened by this rework because it must redirect its current compliance resources away from today's compliance issues.

The *National Taxpayer Advocate's Fiscal Year 1999 Annual Report To Congress* ranked audit reconsiderations 12th out of the 20 most serious problems facing taxpayers today. This was an elevation from the prior year's report, which had ranked audit reconsiderations 19th. According to the 1999 report:

- Taxpayers and their representatives complained that the IRS is neither consistent nor timely in handling requests for audit reconsiderations.
- Audit reconsiderations consistently ranked among the top three major issues of Problem Solving Days,² the Senate Finance Committee, and Taxpayer Advocate Service cases.

While the National Taxpayer Advocate's report indicates an ineffective audit reconsideration process, the volume of tax abatements may indicate a problem with inappropriate audit assessments. The Taxpayer Advocate Service worked approximately 24,000 audit reconsideration cases in FY 1999. The National Taxpayer Advocate said this represents a major problem for taxpayers and it consumes a great deal of Taxpayer Advocate Service resources. The report strongly recommended proactive strategies to reduce audit reconsideration case inventories. This audit was performed to determine whether the IRS effectively gathers and uses information from its audit reconsideration process to increase taxpayer compliance and improve customer service.

¹ An audit reconsideration is a process where the IRS will reconsider the validity of a prior tax assessment. This process provides the taxpayer an opportunity to present information previously not considered during the original audit.

² Problem Solving Days were initiated in November 1997 to provide taxpayers a periodic opportunity for a more personalized, face-to-face contact with an IRS employee who could assist them in resolving their tax problems.

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Results

The IRS does not effectively gather and use information available from the audit reconsideration process to improve its compliance program and increase customer service. As part of the IRS' increased emphasis in this area, a task force was formed to review processes, procedures, and related information in the four program areas³ responsible for audit assessments. The task force found deficiencies in the closure procedures for the original audit assessments and the absence of an information system to track audit reconsideration case trends. One of the task force's recommendations was to develop a management information system to capture pertinent data on audit reconsideration processing. However, the proposed management information reports fall short of senior IRS management expectations. These reports do not measure the total volume of audit reconsideration cases. Specifically, ASFR and AUR assessments are not addressed, even though they make up the majority of audit reconsideration cases worked by the IRS. Identifying the total volume of audit reconsideration cases and their specific causes is essential for developing effective and efficient methods to reduce the number of future audit reconsideration cases. A reduction in the total volume of audit reconsideration cases would directly reduce unnecessary burden on taxpayers and the IRS.

Better Information on Audit Reconsiderations Should Help Reduce Taxpayer Burden

The IRS cannot reduce the burden it causes taxpayers and itself unless it develops an adequate management information system to account for all audit reconsideration cases. The management information reports currently under development⁴ will not accurately capture the total volume of audit reconsideration cases processed by the various functions within the IRS. These reports were being designed to only track audit reconsideration cases currently reopened in the Examination function and any of those cases that are subsequently closed with a full or partial abatement of tax. As a result, these reports will

³ The four areas responsible for audit assessments are: the Automated Substitute for Return (ASFR), the Automated Underreporter (AUR), District Office Examination, and Service Center Correspondence Examination programs. The ASFR program is responsible for securing tax returns from individuals who, based on third-party information, received taxable income and did not file a tax return. The AUR program is responsible for reconciling third-party information to income and certain deductions reported on filed tax returns. The District Office and Service Center Correspondence Examination functions are responsible for the traditional line-item examinations of filed tax returns.

⁴ The development of the management information reports is one of the eight action items related to the national rollout of the centralized audit reconsideration process. The initial reports, scheduled for March 31, 2000, were not operational as of December 2000.

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not account for any audit reconsideration cases worked outside the Examination function or closed without any tax abatement.

Audit reconsideration cases opened outside of the Examination function are primarily related to prior assessments made by the ASFR or AUR programs.⁵ Our analysis showed that approximately 81,000 (76 percent) of the audit reconsideration abatements in FY 1999 were related to prior ASFR or AUR assessments. The IRS cannot reduce the burden it causes to taxpayers and itself unless it develops an adequate management information system to account for all audit reconsideration cases. Without this information, the IRS will not be able to effectively increase compliance and improve customer service.

Summary of Recommendations

We recommend the IRS improve its proposed management information reports to accurately account for the total volume of audit reconsideration cases and to identify their related account characteristics to determine their cause.

Management's Response: IRS Management agreed with our recommendations and stated, "We created a Management Information System (MIS) to provide data from reconsideration cases worked by ASFR, AUR, Appeals, and Examination. We will provide a monthly report to the applicable functions using data from the MIS. Each of the functions will be responsible for reviewing this report to identify trends, including the causes of audit reconsideration, and for developing corrective actions to reduce the volume of future audit reconsideration cases."

⁵ The ASFR and AUR assessments are part of the IRS' Information Reporting Program. This is a computerized program used to match third-party information related to income and certain deductions with the amounts reported by taxpayers on their income tax returns. The IRS also uses the information to identify people who are reported to have received income but did not file a tax return.

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Objective and Scope

Our objective was to determine whether the IRS effectively gathers and uses information from its audit reconsideration process to increase taxpayer compliance and improve customer service.

This audit was initiated as part of the Treasury Inspector General for Tax Administration's coverage to evaluate the effectiveness of the Internal Revenue Service's (IRS) system of controls over the audit reconsideration¹ process. The primary objective of this audit was to determine whether the IRS effectively gathers and uses information from its audit reconsideration process to increase taxpayer compliance and improve customer service.

We evaluated the audit reconsideration process through interviews with analysts and operational personnel in the Collection, Customer Service, and Examination functional processes. We met with analysts from the Taxpayer Advocate Service and the Office of Revenue Analysis to discuss the causes related to audit reconsideration cases. We also performed a review of the centralized audit reconsideration process being prototyped in the service centers and their related field offices.

We conducted our fieldwork in the National Headquarters, the Fresno and Ogden Service Centers, and the Northern California and Pacific-Northwest Districts from May to August 2000. This audit was performed in accordance with *Government Auditing Standards*.

Details of our audit objective, scope, and methodology are presented in Appendix I. Major contributors to this report are listed in Appendix II.

¹ An audit reconsideration is a process where the IRS will reconsider the validity of a prior tax assessment. This process provides the taxpayer an opportunity to present information previously not considered during the original audit.

Audit Reconsideration Cases Create Unnecessary Burden on Taxpayers and the Internal Revenue Service

Background

To prevent needless financial hardship on taxpayers, the IRS instituted a process to reconsider tax assessments made during audits. Discretionary authority is granted to the IRS under the Internal Revenue Code² to abate any unpaid portion of tax where the tax is determined to be excessive. This provides taxpayers the opportunity to request a reduction in the amount of their tax by presenting information not previously considered during the original audit assessments.

Audit reconsiderations have been included as a significant problem in the National Taxpayer Advocate's last three annual reports to the Congress.

As a result of the Senate Finance Committee hearings in September 1997, the IRS instituted Problem Solving Days.³ Audit reconsideration requests were among the most significant problems brought forward by taxpayers at these events and have been included in the National Taxpayer Advocate's last three annual reports to the Congress. The latest report, *National Taxpayer Advocate's Fiscal Year 1999 Annual Report To Congress*, ranked audit reconsiderations 12th out of the 20 most serious problems facing taxpayers today. This was an elevation from the prior year's report, which had ranked audit reconsiderations 19th. According to the 1999 report:

- Taxpayers and their representatives complained that the IRS is neither consistent nor timely in handling requests for audit reconsiderations.
- Audit reconsiderations consistently ranked among the top three major issues of Problem Solving Days, the Senate Finance Committee, and Taxpayer Advocate Service cases.

While the National Taxpayer Advocate's report indicates an ineffective audit reconsideration process, the volume of tax abatements may indicate a problem

² I.R.C. § 6404 (1999).

³ Problem Solving Days were initiated in November 1997 to provide taxpayers a periodic opportunity for a more personalized, face-to-face contact with an IRS employee who could assist them in resolving their tax problems.

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with inappropriate audit assessments. The Taxpayer Advocate Service worked approximately 24,000 audit reconsideration cases in Fiscal Year (FY) 1999. The National Taxpayer Advocate said this represents a major problem for taxpayers and it consumes a great deal of Taxpayer Advocate Service resources. The report strongly recommended proactive strategies to reduce audit reconsideration case inventories.

In January 1998, the IRS Commissioner established the Taxpayer Treatment and Service Improvement Program (TSI).⁴ The TSI created the Audit Reconsideration Task Force in February 1998 to review the IRS' processes, procedures, and related information in the four program areas⁵ responsible for audit assessments. The Task Force noted deficiencies in the closure procedures for the original audit assessments. In addition, it found the IRS did not have a management information system that provided complete or accurate information on the number of audit reconsiderations and their related account characteristics.

The Task Force issued its report in April 1999. The report included recommendations to:

- Reaffirm, as IRS policy, a taxpayer's right to request and receive an audit reconsideration.
- Improve the locator processes for taxpayers prior to assessing tax.

⁴ The TSI coordinates, through specific initiatives, improvements to the way the IRS provides service to taxpayers. Audit reconsiderations is currently one of its initiatives.

⁵ The four areas responsible for audit assessments are: the Automated Substitute for Return (ASFR), the Automated Underreporter (AUR), District Office Examination, and Service Center Correspondence Examination programs. The ASFR program is responsible for securing tax returns from individuals who, based on third-party information, received taxable income and did not file a tax return. The AUR program is responsible for reconciling third-party information to income and certain deductions reported on filed tax returns. The District Office and Service Center Correspondence Examination functions are responsible for the traditional line-item examinations of filed tax returns.

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- Centralize the audit reconsideration process in each service center.
- Develop a management information system to capture and report data pertinent to audit reconsideration processing.

The TSI Executive Steering Committee⁶ immediately approved these recommendations. In September 1999, the IRS issued Policy Statement P-2-89, which reaffirms a taxpayer's right to request an audit reconsideration of an unpaid tax assessment. To reduce the number of excessive tax assessments, both the Customer Service and Examination functions have enhanced their locator procedures and discontinued assessing tax on the accounts of unlocatable taxpayers.⁷ The Audit Reconsideration Task Force noted the success of the centralized audit reconsideration processes being prototyped in the Fresno and Ogden Service Centers. As a result, the IRS committed to a nationwide rollout of a centralized audit reconsideration process in the beginning of FY 2001.

Results

Audit reconsideration cases create an unnecessary burden on both the taxpayers and the IRS.

Audit reconsideration cases create an unnecessary burden on both the taxpayers and the IRS. In FY 1999 alone, the IRS abated audit assessments on the accounts of approximately 106,000 individual taxpayers through its audit reconsideration process. This represents a burden on taxpayers because it requires them to address

⁶ The IRS Commissioner chairs the TSI Executive Steering Committee. It (1) provides authoritative and timely decisions on all matters that affect implementation of TSI commitments and recommendations and (2) ensures that all major corporate level commitments made to external stakeholders and implementation of recommendations from either internal or external sources are consistent with the IRS' business strategy.

⁷ Some instances when an assessment for an unlocatable taxpayer would be appropriate are (1) the return has significant unreported income, (2) voluntary compliance would be undermined by not assessing the tax, and (3) there is a credit balance on the taxpayer's account.

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excessive tax assessments that should have been resolved during the initial audit. The IRS is also burdened by this rework because it must redirect its current compliance resources away from today's compliance issues.

The IRS cannot address the problems related to audit reconsiderations because it does not effectively gather and use information available from the audit reconsideration process. Without an adequate management information and reporting system, the IRS cannot track these cases, determine their causes, and implement measurable corrective actions that will reduce their number and ultimately decrease taxpayer burden.

Better Information on Audit Reconsiderations Should Help Reduce Taxpayer Burden

Management accountability is the expectation that managers are responsible for mitigating adverse aspects of agency operations.⁸ The IRS cannot reduce the burden caused by audit reconsideration cases because it does not have an adequate management information system from which to make informed decisions. The IRS needs an effective system for tracking case trends to determine their cause and for developing corrective actions to reduce the number of audit reconsideration cases it processes each year.

The Office of Revenue Analysis is in the process of developing monthly reports⁹ that forecast audit reconsideration trends and plan for resource allocations. These reports were to be part of the regular Enforcement

⁸ Office of Management and Budget Circular A-123.

⁹ The development of the management information reports is one of the eight action items related to the national rollout of the centralized audit reconsideration process. The initial reports, scheduled for March 31, 2000, were not operational as of December 2000.

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Revenue Information System (ERIS)¹⁰ production. However, the proposed management information reports fall short of senior IRS management expectations and do not capture information on all audit reconsiderations. These reports were designed to track only those audit reconsideration cases currently reopened in the Examination function and any of those cases that are subsequently closed with a full or partial abatement of tax. By tracking only these cases, the reports do not capture information for the majority of audit reconsideration cases. The audit reconsideration cases not included are those:

- Reopened outside the Examination function.
- Closed without an abatement of prior tax assessments.

Information is not captured on audit reconsideration cases reopened outside the Examination function

The proposed management information reports will not account for audit reconsideration cases where the requests are related to a prior ASFR or AUR tax assessment.

Most audit reconsideration requests opened outside the Examination function are related to ASFR and AUR assessments. According to the IRS, these accounts were not included in the design of the ERIS reports because they are not a true reconsideration of audit tax issues. Instead, these are situations where the IRS has third-party information showing the taxpayer had taxable income and either did not file a return or omitted income from his/her filed return. This contradicts the fact that the *National Taxpayer Advocate's Fiscal Year 1999 Annual Report To Congress* stated that a large number of audit reconsideration cases were the result of assessments made through the ASFR program.

Our analysis showed that the IRS processed audit reconsideration tax abatements on the accounts of approximately 106,000 individual taxpayers in FY 1999.

¹⁰ The Office of Revenue Analysis administers the ERIS. The ERIS is a cross-functional database that tracks the amount and timing of revenue from all IRS enforcement actions.

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These abatements totaled over \$711 million.¹¹ In addition, we determined that approximately 81,000 (76 percent) of these accounts were audit reconsideration abatements to ASFR or AUR assessments.

Information is not captured on audit reconsideration cases closed without an abatement of prior tax assessments

The true number of audit reconsideration cases closed by the IRS is unknown.

When taxpayers request an audit reconsideration but do not provide documentation or the documentation provided does not support a reduction in tax, the cases are closed by the IRS without an abatement. In these situations, the IRS does not retain any specific information that shows an audit reconsideration request was processed or even received. As a result, the true number of audit reconsideration cases closed by the IRS is unknown.

However, the Taxpayer Advocate Management Information System (TAMIS)¹² does track some audit reconsideration information on a very limited basis. We determined that the Taxpayer Advocate Service closed approximately 24,000 individual taxpayer audit reconsideration cases in FY 1999.¹³ Approximately 17,000 (71 percent) of these cases were closed without an abatement of tax.

Most audit reconsideration cases closed without an abatement of tax would still involve a significant investment of IRS resources. At a minimum, these types of case closures would require some form of taxpayer contact. A case that is ultimately denied would

¹¹ As the IRS did not track the total volume of audit reconsideration cases, our analysis assumed that any tax abatement following the original audit assessment was the result of an audit reconsideration request.

¹² The TAMIS is a database used to control and track every taxpayer case worked by the Taxpayer Advocate Service. It tracks and counts the volume of all audit reconsideration cases worked regardless of tax abatement.

¹³ We did not validate the accuracy of the information provided by the IRS in this download.

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The IRS is currently not able to accurately track case trends to forecast and plan for resource allocations, identify the causes of audit reconsiderations, or measure effectiveness of corrective actions.

generally require a review of the circumstances leading to the prior assessment, as well as a review of any new supporting documentation.

The IRS needs to accurately track case trends for all audit reconsideration cases, regardless of their final resolution, in order to:

- Identify the specific causes.
- Develop corrective actions to reduce audit reconsiderations.
- Measure the effectiveness of implemented corrective actions.
- Forecast and plan for sufficient resource allocations.

The IRS cannot provide top quality service to taxpayers unless it has the ability to track the causes of audit reconsideration cases. The IRS needs the ability to determine whether there are systemic problems with current audit assessment procedures or whether a lack of taxpayer education is responsible for the large number of audit reconsideration requests. A reduction in the total volume of audit reconsideration cases would directly reduce unnecessary burden on taxpayers and the IRS.

Recommendation

1. The IRS should redesign its management information reports to account for all audit reconsideration cases. These reports need to include all audit reconsideration requests, regardless of which function processes them, and identify whether the case was closed with or without an abatement of tax. Once the IRS has accounted for all audit reconsideration cases, it needs to track the case trends to identify the causes of the audit reconsideration cases, their final dispositions, and the resources it uses to process the cases. This information should then be used to develop effective corrective actions to reduce the total volume of future audit reconsideration cases.

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Management's Response: IRS Management agreed with our recommendations and stated, "We created a Management Information System (MIS) to provide data from reconsideration cases worked by ASFR, AUR, Appeals, and Examination. We will provide a monthly report to the applicable functions using data from the MIS. Each of the functions will be responsible for reviewing this report to identify trends, including the causes of audit reconsideration, and for developing corrective actions to reduce the volume of future audit reconsideration cases."

Conclusion

Audit reconsideration cases create an unnecessary burden on both the taxpayer and the IRS. The taxpayer is faced with a tax liability that may be incorrect, while the IRS is faced with redirecting compliance resources to rework cases. The IRS will not be able to correct the problems caused by audit reconsiderations unless it has an adequate management information system to track these cases and determine their causes. With this in place, the IRS will be better able to develop corrective actions that increase taxpayer compliance and improve customer service.

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Appendix I

Detailed Objective, Scope, and Methodology

The primary objective of this audit was to determine whether the Internal Revenue Service (IRS) effectively gathers and uses information from its audit reconsideration¹ process to increase taxpayer compliance and improve customer service. To accomplish this objective, we:

- I. Interviewed analysts from the Taxpayer Advocate Service function to discuss any concerns with the audit reconsideration process. Interviewed analysts and operational personnel from the Collection, Customer Service, and Examination functions to determine whether there was effective oversight of the audit reconsideration process. Specifically, identified:
 - A. Management's oversight role, the involvement of the current issue owner for the audit reconsideration process, and the policies and procedures for processing audit reconsideration cases.
 - B. The management information systems in place to measure, monitor, and account for audit reconsideration activities.
 - C. The methodologies used to ensure new policies and procedures have the intended results on the audit reconsideration process.
- II. Interviewed analysts from the Office of Revenue Analysis and the Taxpayer Advocate Service functions, as well as analysts and operational personnel from the Collection, Customer Service, and Examination functions, to determine whether the IRS had a process in place to identify the causes of audit reconsideration cases.
- III. Interviewed analysts from the Office of Revenue Analysis and Taxpayer Advocate Service functions, as well as analysts and operational personnel from the Collection, Customer Service, and Examination functions, to determine whether the IRS had a system in place to measure the effectiveness and efficiency of the audit reconsideration process.

¹ An audit reconsideration is a process where the IRS will reconsider the validity of a prior tax assessment. This process provides the taxpayer an opportunity to present information previously not considered during the original audit.

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- IV. Determined whether the IRS effectively and efficiently implemented the Audit Reconsideration Task Force recommendations. Specifically:
 - A. Identified the recommendations and determined whether they were timely implemented.
 - B. Evaluated the centralized audit reconsideration processes being prototyped in the Fresno and Ogden Service Centers.
 - C. Reviewed the action plan for centralizing the audit reconsideration process in the service centers and determined whether the established implementation timelines were being met.
- V. Quantified the outcome measures related to taxpayer rights and burden by performing the following steps:
 - A. Secured information from the Taxpayer Advocate Management Information System (TAMIS)² database and determined that the Taxpayer Advocate Service function processed 23,656 audit reconsideration cases in Fiscal Year (FY) 1999 (October 1, 1998, through September 30, 1999).
 - B. Analyzed the Individual Masterfile (IMF)³ and determined the IRS had processed audit reconsideration tax abatements to 105,617 taxpayer accounts in FY 1999. The case population included all abatements to the Automated Substitute for Return (ASFR), the Automated Underreporter (AUR),⁴ District Office Examination, and Service Center Correspondence Examination functions.
 - C. Interviewed analysts from the Office of Revenue Analysis to determine the status of the audit reconsideration management information reports.
 - D. Matched the 23,656 taxpayer accounts from the TAMIS database to the IMF. Determined that the Taxpayer Advocate Service function processed audit reconsideration cases with tax abatements to 6,862 taxpayer accounts and closed 16,794 cases without a tax abatement.

² The TAMIS is a database used to control and track every taxpayer case worked by the Taxpayer Advocate Service. It tracks and counts the volume of all audit reconsideration cases worked regardless of tax abatement.

³ The IMF is an extensive IRS database containing tax return information for individual income tax return filers.

⁴ The ASFR and AUR assessments are part of the IRS' Information Reporting Program. This is a computerized program used to match third-party information related to income and certain deductions with the amounts reported by taxpayers on their income tax returns. The IRS also uses the information to identify people who are reported to have received income but did not file a tax return.

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Appendix II

Major Contributors to This Report

Walter E. Arrison, Associate Inspector General for Audit (Wage and Investment Income Programs)

Michael Phillips, Director

Stan Rinehart, Director

Bryce Kisler, Audit Manager

Alan Lund, Senior Auditor

Sharon Summers, Senior Auditor

Jim Traynor, Senior Auditor

Erin Kaauwai, Auditor

Kristi Larson, Auditor

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Appendix III

Report Distribution List

Deputy Commissioner N:DC
Commissioner, Small Business/Self-Employed Division S
Commissioner, Wage and Investment Division W
Deputy Commissioner, Small Business/Self-Employed Division S
Deputy Commissioner, Wage and Investment Division W
Director, Compliance S:C
Director, Compliance W:CP
Director, Research, Analysis and Statistics of Income N:ADC:R
Director, Strategy and Finance W:S
Director, Legislative Affairs CL:LA
National Taxpayer Advocate TA
Office of Management Controls N:CFO:F:M
Office of the Chief Counsel CC
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O
Audit Liaisons:
 Deputy Commissioner N:DC
 Commissioner, Small Business/Self-Employed Division S
 Commissioner, Wage and Investment Division W
 National Taxpayer Advocate TA
 Senior Operations Advisor W:S

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Appendix IV

Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

Type and Value of Outcome Measure:

- Taxpayer Burden – Potential; 106,000 taxpayer accounts affected; see page 6.

Methodology Used to Measure the Reported Benefit:

We analyzed an extract from the Internal Revenue Service's Individual Masterfile¹ for any assessments with abatements processed in Fiscal Year 1999.

¹ The IMF is an extensive IRS database containing tax return information for individual income tax return filers.

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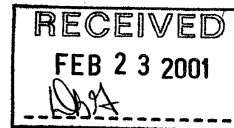
Appendix V

Management's Response to the Draft Report



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

FEB 23 2001



MEMORANDUM FOR TREASURY INSPECTOR GENERAL FOR TAX
ADMINISTRATION

FROM:

Joseph G. Kehoe 
Commissioner, Small Business/Self-Employed Division

SUBJECT:

Draft Report - "Audit Reconsideration Cases Create
Unnecessary Burden on Taxpayers and the Internal Revenue
Service" (Audit #2000-40-042)

I appreciate the opportunity to respond to your draft report, "Audit Reconsideration Cases Create Unnecessary Burden on Taxpayers and the Internal Revenue Service." I agree with your recommendation that our management information reports should account for all reconsideration cases. We established a tracking system for reconsideration cases in early 2000; however, we quickly recognized that it was not capturing all the data. Since then, we have been working with the Office of Revenue Analysis to develop a report that will include reconsideration cases from the Automated Underreporter program (AUR), the Automated Substitute for Return program (ASFR), Appeals and Examination (Reporting Compliance). The first report is scheduled for March 31, 2001.

I am pleased to tell you our recent changes in the reconsideration process have affected how this issue was ranked in the *Taxpayer Advocate's Fiscal Year 2000 Annual Report to Congress*. This year the issue of reconsideration ranked 18th out of 20th of the most serious problems facing taxpayers today. Last year's report ranked the reconsideration process as 12th out of 20th.

We will continue to reduce the burden on taxpayers and the IRS by centralizing the reconsideration process, improving locator procedures, and using unique P.O. boxes to decrease the chance of misrouted mail.

Our comments on your recommendation are as follows:

IDENTITY OF RECOMMENDATION 1

The IRS should redesign its management information reports to account for all audit reconsideration cases. These reports need to include all audit reconsideration requests, regardless of which function processes them, and identify whether the case was closed with or without an abatement of tax. Once the IRS has accounted for all

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audit reconsideration cases, it needs to track the case trends to identify the causes of the audit reconsideration cases, their final dispositions, and the resources it uses to process the cases. This information should be used to develop effective corrective actions to reduce the total volume of future audit reconsideration cases.

ASSESSMENT OF CAUSE

We did not capture all reconsideration cases, such as those related to a prior AUR tax assessment, in management information reports. The true volume of reconsideration cases was not readily apparent to the IRS.

CORRECTIVE ACTION

We created a Management Information System (MIS) to provide data from reconsideration cases worked by ASFR, AUR, Appeals and Examination. We will provide a monthly report to the applicable functions using data from the MIS. Each of the functions will be responsible for reviewing this report to identify trends, including the causes of audit reconsideration, and for developing corrective actions to reduce the volume of future audit reconsideration cases.

IMPLEMENTATION DATE

Proposed (delivery of the first monthly MIS report): March 31, 2001

Proposed (monitor report/identify trends): Ongoing but will begin in April 2001

RESPONSIBLE OFFICIAL

Director, Compliance, Small Business/Self-Employed
Director, Compliance, Wage and Investment

CORRECTIVE ACTION MONITORING PLAN

Small Business/Self-Employed and Wage and Investment will work closely with the Office of Revenue Analysis to ensure monthly delivery of the report. Both Divisions will analyze the data on a monthly basis to determine trends and to identify potential corrective actions.

If you have any questions about this response, please contact Glenn E. Henderson, Director, Compliance, Small Business/Self-Employed at (202) 622-5100.